

Legislative Audit Division

State of Montana



Report to the Legislature

April 1999

Financial Audit

For the Fiscal Year Ended June 30, 1998

Montana Water Pollution Control and Drinking Water State Revolving Fund Programs

**Department of Environmental Quality
Department of Natural Resources and Conservation**

We performed a financial audit of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs for the fiscal year ended June 30, 1998. This report contains the audited financial statements and accompanying notes for fiscal year 1997-98. We issued an unqualified opinion on the financial statements. The opinion means the reader may rely on the financial statement information presented.

Direct comments/inquiries to:
**Legislative Audit Division
Room 135, State Capitol
PO Box 201705
Helena MT 59620-1705**

99SP-48

Help eliminate fraud, waste, and abuse in state government. Call the Fraud Hotline at 1-800-222-4446 statewide or 444-4446 in Helena.

FINANCIAL AUDITS

Financial audits are conducted by the Legislative Audit Division to determine if an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States General Accounting Office. Financial audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Legislative Audit Division
Room 135, State Capitol
PO Box 201705
Helena MT 59620-1705

MEMBERS OF THE LEGISLATIVE AUDIT COMMITTEE

Senator Linda Nelson, Chair	Representative Bruce Simon, Vice Chair
Senator Sue Bartlett	Representative Beverly Barnhart
Senator Reiny Jabs	Representative Ernest Bergsagel
Senator Tom Keating	Representative A. R. "Toni" Hagener
Senator Ken Miller	Representative Robert Pavlovich
Senator Barry "Spook" Stang	Vacant

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel
Tori Hunthausen, IT & Operations Manager



Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
James Gillett, Financial-Compliance Audit

April 1999

The Legislative Audit Committee
of the Montana State Legislature:

This is our report on the fiscal year 1997-98 financial audit of the Montana Water Pollution Control State Revolving Fund (WPCSRF) and Drinking Water State Revolving Fund (DWSRF) Programs. The Department of Natural Resources and Conservation requested the initial audit of these programs because annual audits are now required by the Environmental Protection Agency.

The objectives of a financial audit include determining if the programs' financial statements present fairly its financial position at June 30, 1998, and the results of its operation for the fiscal year then ended. We tested compliance with state and federal laws that have a direct and material impact on the financial statements.

The WPCSRF program provides loans at a reduced interest rate to finance construction of publicly-owned water pollution control facilities, non-point source pollution control projects, and estuary management plans. Water Pollution control loans must be repaid within 20 years. As of June 30, 1998, the Water Pollution Control Program had \$35,510,667 of outstanding loans.

The DWSRF will make low interest loans to communities for the construction of drinking water treatment facilities. At June 30, 1998, the Drinking Water Program was in a start-up phase and had not issued any loans. These loans will be required to be repaid within 30 years. The departments expect to begin issuing Drinking Water Loans in fiscal year 1998-99.

On page A-1, you will find the Independent Auditor's Report followed by the financial statements and accompanying notes. We issued an unqualified opinion which means the reader can rely on the presented information. The programs' financial statements begin on page A-3. Our opinion on the program's supplementary financial information is on page B-1. The supplementary information begins on page B-3. Beginning on page C-1 is our report on compliance and internal control which is required by *Government Auditing Standards* issued by the Controller General of the United States.

We thank the directors of the Department of Environmental Quality and the Department of Natural Resources and Conservation and their staff for cooperation and assistance during the audit.

Respectfully submitted,

(Signature on file)

Scott A. Seacat
Legislative Auditor

Appointed and Administrative Officials

**Department of
Environmental Quality**

Mark Simonich, Director

David Thorsen, Administrator, Centralized Services Division

Tom Livers, Chief, Technical and Financial Assistance Bureau

**Department of Natural
Resources and
Conservation**

Bud Clinch, Director

Anna Miller, Financial Advisor

Ann Bauchman, Administrator, Centralized Services Division

For additional information concerning the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs, contact Anna Miller, Financial Advisor, at:

PO Box 201601
Helena MT 59620-1601
(406) 444-6689

e-mail: amiller@state.mt.us

The audit staff involved in this audit was Wayne Guazzo

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel
Tori Hunthausen, IT & Operations Manager



Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

To the Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Combined Balance Sheet of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs, as of June 30, 1998, and the related Combined Statement of Revenues, Expenditures, and Changes in Fund Balance for the year then ended. These financial statements are the responsibility of management at the Montana Department of Environmental Quality and the Montana Department of Natural Resources and Conservation. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and Government Auditing Standards issued by the Controller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in the notes to the financial statements, the financial statements of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs are intended to present the financial position and results of operations of only that portion of the financial reporting entity of the State of Montana that is attributable to the transactions of the programs.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs, as of June 30, 1998, and the results of its operations for the year then ended in conformity with generally accepted accounting principles.

This report is intended for the information and use of the Legislative Audit Committee, department management, the Montana State Legislature, and the U.S. Environmental Protection Agency and should not be used by anyone other than these specified parties. This report is a matter of public record and its distribution is not limited.

Respectfully submitted,

(Signature on file)

James H. Gillett, CPA
Deputy Legislative Auditor

March 12, 1999

**MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
STATE REVOLVING FUND PROGRAMS
COMBINED BALANCE SHEET
JUNE 30, 1998**

	WATER POLLUTION CONTROL		DRINKING WATER	(FOR MEMORANDUM ONLY) TOTAL
	SPECIAL REVENUE	DEBT SERVICE	SPECIAL REVENUE	
ASSETS				
Cash/Cash Equivalents	\$1,678,284	\$465,631	\$54,365	\$2,198,280
Due From Other Accounting Entities	10,618		55,035	65,653
Interest Receivable	81,491	337,859		419,350
Due from Federal Government			264,461	264,461
Investments	11,901,366	1,069,692		12,971,058
Loans Receivable	35,510,667			35,510,667
Total Assets	<u>\$49,182,426</u>	<u>\$1,873,182</u>	<u>\$373,861</u>	<u>\$51,429,469</u>
LIABILITIES AND FUND BALANCES				
<i>Liabilities:</i>				
Deferred Revenue	\$233,463			\$233,463
Accounts Payable	373		\$798	1,171
Due to Other Accounting Entities	17,818		23,063	40,881
Interentity Loans Payable			350,000	350,000
Total Liabilities	<u>251,654</u>		<u>373,861</u>	<u>625,515</u>
<i>Fund Balances</i>				
Reserved for Loans Receivable	35,510,667			35,510,667
Unreserved, Undesignated	13,420,105	<u>\$1,873,182</u>	0	15,293,287
Total Fund Balances	<u>48,930,772</u>	<u>1,873,182</u>	0	<u>50,803,954</u>
Total Liabilities and Fund Balances	<u>\$49,182,426</u>	<u>\$1,873,182</u>	<u>\$373,861</u>	<u>\$51,429,469</u>

The accompanying notes to the financial statements are an integral part of this statement.

**MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
STATE REVOLVING FUND PROGRAMS
COMBINED STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
FOR THE YEAR ENDING JUNE 30, 1998**

	<u>WATER POLLUTION CONTROL</u>	<u>DRINKING WATER</u>	<u>(FOR MEMORANDUM ONLY) TOTAL</u>
	<u>SPECIAL REVENUE</u>	<u>DEBT SERVICE</u>	<u>SPECIAL REVENUE</u>
REVENUES:			
Federal Capitalization Grant Revenue	\$5,864,005		\$233,432
Interest Income on Investments	643,432	72,900	716,332
Interest Earnings	246,757	1,045,559	1,292,316
Administration and Origination Fees	126,456		126,456
TOTAL REVENUES	6,880,650	1,118,459	8,232,541
EXPENDITURES:			
Program Administration	261,691		233,432
State In-Kind Services-RIT	10,853		10,853
TOTAL EXPENDITURES	272,544		233,432
			505,976
Excess Revenues Over/(Under) Expenditures	6,608,106	1,118,459	0
			7,726,565
OTHER FINANCING SOURCES:			
GO 98A Bond Proceeds	3,510,000		3,510,000
<i>Operating Transfers In:</i>			
Debt Service Sweep	109,889		109,889
Origination/Administrative Fee Transfer		80,290	80,290
RIT Transfers In	10,853		10,853
Arbitrage Rebate Transfer	31,575		31,575
Total Other Financing Sources	3,630,742	111,865	0
			3,742,607
OTHER FINANCING USES:			
Bond Principal		200,000	200,000
Bond Interest		409,429	409,429
Bond Cost of Issuance	96,773		96,773
<i>Operating Transfers Out:</i>			
Debt Service Sweep		109,889	109,889
Origination/Administrative Fee Transfer	80,290		80,290
Arbitrage Rebate Transfer	31,575		31,575
Total Other Financing Uses	208,638	719,318	927,956
Excess(deficiency) of revenues and other financing sources over(under) expenditures and other financing uses	10,030,210	511,006	10,541,216
Fund Balance - July 1, 1997	38,879,623	1,362,176	0
Prior Period Adjustments	20,939		20,939
Fund Balance - July 1, 1997--As Restated	<u>38,900,562</u>	<u>1,362,176</u>	<u>0</u>
Fund Balance - June 30, 1998	<u>\$48,930,772</u>	<u>\$1,873,182</u>	<u>\$0</u>
			<u>\$50,803,954</u>

The accompanying notes to the financial statements are an integral part of this statement.

**MONTANA STATE WATER POLLUTION CONTROL AND DRINKING
WATER STATE REVOLVING FUND PROGRAMS
SPECIAL REVENUE AND DEBT SERVICE FUND
NOTES TO FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 1998**

1. Organization of the Programs

The State of Montana's Water Pollution Control State Revolving Fund (WPCSRF) Program was established pursuant to Title VI of the Federal Water Quality Act of 1987. This federal act established the WPCSRF program to replace the construction grants program to provide a flexible financing source to loan money at reduced interest rates to finance the construction of publicly owned water pollution control facilities, non-point source pollution control projects, and estuary management plans. Instead of making grants to communities that pay for a portion of building wastewater treatment facilities, the WPCSRF provides for low interest rate loans to finance the entire cost of qualified projects.

The State of Montana's Drinking Water State Revolving Fund (DWSRF) Program was established pursuant to Title XIV of the Safe Drinking Water Act. This federal act established the DWSRF program for states to make loans to community water systems and nonprofit non-community water systems. Instead of making grants to communities that pay for a portion of building drinking water treatment facilities, the DWSRF provides for low interest rate loans to finance the entire cost of qualified projects or to refinance debt obligations on projects, which began after July 1, 1993. The State of Montana first incurred expenditures in the DWSRF Program in FY 1997. This program was in a start-up phase and had not issued any loans as of June 30, 1998.

WPCSRF Loans must be repaid within 20 years, while DWSRF loan agreements allow up to 30 years for repayment. All repayments of interest and principal must remain in the Fund.

Both programs are capitalized through U.S. Environmental Protection Agency (EPA) grants. States are required to provide an additional 20 percent of the Federal capitalization grant as matching funds in order to receive a grant.

The programs are administered jointly by the Department of Environmental Quality (DEQ) Technical and Financial Assistance Bureau, and the Department of Natural Resources and Conservation (DNRC) Conservation and Resource Development Division. The fund does not have any full time employees. Both funds are charged for time spent on SRF activities by department employees. The charges include salaries and benefits of the employees and operating expenses, as well as indirect costs.

2. Summary of Significant Accounting Policies

A. SRF Program Fund Structure

Both programs use Special Revenue and Debt Service funds, as appropriate, to report their financial position and the results of operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions and activities. Montana maintains a State Special Revenue and a Federal Special Revenue Fund. The SRF programs are blended from a part of each Special Revenue Fund. A fund is a separate accounting entity with a self-balancing set of accounts. Special Revenue and Debt Service funds are considered governmental funds.

A Special Revenue Fund accounts for the proceeds of specific revenue sources restricted to expenditure for specified purposes (other than expendable trusts or major capital projects). A Debt Service Fund accounts for resources accumulated for payment of principal and interest on general long-term obligation debt.

B. Basis of Accounting

The accounting and reporting treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for on a current financial resources measurement focus. Only assets and current liabilities are generally included on their balance sheets. Governmental fund operating statements present increases(revenues and other financing sources) and decreases(expenditures and other financing uses) in net current assets.

These funds use the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recorded when received in cash unless susceptible to accrual. Revenues are susceptible to accrual if they are measurable and available to finance expenditures of the fiscal period or are not received at the normal time of receipt. Revenues are deferred if material and received before the normal time of receipt or if received for a particular activity and the expense for that activity has not been incurred prior to fiscal year-end. Expenditures are recognized when the related fund liability is incurred, with the following exceptions:

- 1) principal and interest on long-term debt is recognized when due;
- 2) prepayments are accounted for as expenditures in the period of acquisition;
- 3) inventory items are considered expenditures when purchased.

3. Cash/Cash Equivalents

Cash and cash equivalents consist of funds deposited with the Montana State Treasurer, and investments categorized as cash equivalents, which are short-term, highly liquid investments with original maturities of three months or less.

<u>Risk Category 1</u>	<u>Carrying Amount</u>	<u>Fair Value</u>	<u>Fund</u>
Money Market Direct Investment	\$2,091,635	\$2,091,635	various

4. Due from Federal Government

This classification consists of amounts expended and awaiting receipt of the Federal Capitalization Grant Reimbursement.

5. Investments

The Board of Examiners of the State of Montana authorizes the sale of general obligation bonds to provide the state match for the programs through the issuance of an Indenture of Trust. The Board of Examiners is comprised of the Governor, Attorney General, and the Secretary of State for the State of Montana. The Indenture of Trust specifies the eligible investments meeting defined rating and risk criteria in which the state may invest. The state invests funds through its Trustee Bank, US Bank, N.A. of Billings.

Security Type	Category 1	Category 2	Category 3	Carrying Amount	Market Value
Government Securities	\$12,806,417			\$12,806,417	\$12,971,058

6. Loans Receivable

Montana operates both SRF programs as direct loan programs. Loans made to communities through the Water Pollution Control Program are 83.3 percent funded by the Federal Capitalization grant, and 16.7 percent by the state match amount. Loans made by the Drinking Water Program are funded 80% by the Federal Capitalization grant, and 20% by the state match amount. Loan funds are disbursed to the local agencies by the trustee bank as local agencies expend funds for the purposes of the loan, and request reimbursement from the program. Interest is calculated from the date that funds are advanced. Typically after the final disbursement has been made, the payment schedule is certified in the loan agreement and adjusted for the actual amounts disbursed. No provision for uncollectible accounts has been made as all loans are current, and management believes that all loans will be repaid according to the loan terms.

In the WPCSRF one loan to the community of Glendive is a refinanced loan with a carrying value of \$225,000. The outstanding principal balance of all loans guaranteed by the WPCSRF program as of June 30, 1998, is \$35,510,667.

Loans mature at various intervals through July 1, 2018. The scheduled principal payments on loans maturing in years after 1998 are as follows:

<u>Year ending June 30:</u>	<u>Amount</u>
1999	\$ 1,385,970
2000	1,845,000
2001	3,787,000
2002	3,264,000
2003 and thereafter	<u>25,228,697</u>
Total	\$35,510,667

As of June 30, 1998 the Fund had authorized loans to public entities of the state of Montana that in the aggregate exceeded \$32 million. The outstanding balances of these loans represent approximately 89% of the total loans receivable. The outstanding balances of the largest ten loans are as follows.

<u>Local Agency</u>	<u>Authorized Loan Amount</u>	<u>Outstanding Balance</u>
Big Sky County Water & Sewer	\$5,513,000	\$5,252,971
City of Butte-Silver Bow	5,307,390	4,144,390
City of Kalispell	4,717,000	3,114,000
Flathead County Evergreen	3,600,000	2,980,000
City of Missoula Reserve Street	2,496,000	1,806,000
City of Missoula W/B Clarifier	2,465,000	1,466,000
City of Havre	2,224,000	130,732
Missoula Cty. Linda Vista RSID	2,022,000	1,419,000
City of Troy	1,824,000	1,504,828
City of Dillon	<u>1,856,000</u>	<u>1,580,925</u>
Total	\$32,024,390	\$23,398,846

7. Interest Receivable

This account represents interest owed by borrowers for their July 1998 payment as of June 30, 1998. It represents the six months of interest accrued from the loan payment made in January 1998, minus \$252,270 of interest received in June, that was due in July 1998.

8. Interentity Loans Payable

Interentity Loans Payable are amounts owed another state account within the Department of Environmental Quality. This money was borrowed to provide temporary capital in advance of receipt of the DWSRF federal capitalization grant.

9. Bonds Payable

General Obligation Debt—Wastewater Treatment Works

<u>Principal Payments</u>					
Series	Amount Issued	Int. Range(%)	FY99	In Year of Maturity	Balance June 30, 1998
1991B	\$ 2,595,000	5.6-6.8	\$ 85,000	\$215,000 (2014)	\$ 2,235,000
1994B	\$ 2,200,000	4.6-6.1	70,000	\$180,000 (2016)	\$ 2,070,000
1996C	\$ 2,765,000	4.2-5.75	100,000	\$120,000 (2017)	\$ 2,710,000
1998A	<u>\$ 3,510,000</u>	<u>3.75-5.15</u>	<u>0</u>	<u>\$260,000 (2019)</u>	<u>\$ 3,510,000</u>
Total	\$11,070,000		\$255,000		\$10,525,000

Debt Service Requirements (principal and interest) for SRF are as follows:

<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004+</u>	<u>Totals</u>
\$789,876	\$932,080	\$928,639	\$928,847	\$927,660	\$12,272,340	\$16,779,442

Interest earnings from both programs have been and will be used to liquidate this long-term debt. Year of maturity refers to fiscal year. The General Obligation Bonds Payable are blended into the General Long Term Obligations Account Group on the State of Montana Comprehensive Annual Financial Report (CAFR) and are not included on the program's financial statements.

10. Fund Balance

A portion of the fund balance in the WPCSRF has been reserved for Loans Receivable indicating that a portion of the fund balance is not available for expenditure.

The WPCSRF is capitalized by grants from EPA and matching funds from the State of Montana. All grant funds drawn are recorded as revenue. As of June 30, 1998, EPA has awarded capitalization grants of \$60,082,200 to the State of Montana, of which \$37,034,791 has been drawn for loans and administrative expenses. Montana has issued bonds totalling \$11,070,000, for use as state matching funds.

The first year of operation for the DWSRF program was in FY 97. At fiscal year-end 1997, the fund balance in this account was zero. In FY 97 the DWSRF incurred \$45,902 in expenditures, of which \$14,872 was funded by state RIT resources and the balance of \$31,030 will be funded through the SRF account. In FY 97, an interentity loan of \$50,000 was made available within DEQ to fund these expenditures in advance of the grant. In FY 98, an additional \$300,000 interentity loan was made to continue DWSRF operations. On June 23, 1998, the State of Montana was awarded its first capitalization grant for the DWSRF program for \$14,826,200.

11. Federal Capitalization Grant Revenues

Actual draws of federal funds differed from the amount reported on the Statement of Revenues, Expenditures, and Changes in Fund Balance. This occurs because state accounting policy requires that federal special revenue accounts reflect a zero fund balance at fiscal year-end. Consequently, if a positive fund balance exists, a deferred revenue is recorded. If a negative fund balance is reflected at fiscal year-end, a revenue accrual to record revenue is recorded to zero the fund balance. In FY 98, revenues were deferred to zero out a positive fund balance.

WPCSRF federal draws are reconciled as follows:

Federal Cap. Grant Revenue on General Ledger:	\$ 5,864,005
FY 98 Deferred Revenue Increase	233,463
FY 97 Deferred Revenue Decrease	(12,859)
DNRC Indirect Charge—Revenue Abatement	208
Total Federal Draws	\$ 6,084,817

12. Interest Income on Investments

This revenue represents interest earnings on investments in the various accounts within the fund. All assets of the fund are invested to the degree possible by the trustee in various investment vehicles, ranging from cash equivalents to long term investments.

13. Interest Earnings

This revenue represents interest earnings from loan repayments made by borrowers.

14. Program Administration

This expenditure represents costs incurred by DEQ and DNRC to administer the SRF programs. This amount is limited to 4% of each grant award from the EPA. Program Administration appears under the Resource Development/Recreation function in the State of Montana's CAFR.

15. Other Financing Sources and Uses

Loan interest amounts received that exceed the debt service requirements are shown as a Financing Source and a Use on the financial statements. The balance remaining in the Debt Service Account is transferred to the Investment Account. Both accounts are within the same program. This occurs after payments are rendered to the bondholders on July 15 of each year. In the Arbitrage Certificate, this activity is termed a Debt Service Sweep.

Administration and Origination Fees are shown both as a Financing Source and Use of funds because the fees are initially recorded inside the loan account when disbursed.

These revenues are then transferred to the Special Administration and Loan Loss Reserve Accounts, which are outside the fund.

RIT Transfers In represent financial support provided to the programs utilizing state Resource Indemnity Trust (RIT) monies and are considered match dollars for the WPCSRF program.

The Arbitrage Rebate Transfer reflects monies transferred into the Rebate Account (outside the fund) based on the annual arbitrage rebate liability calculation.

16. Subsequent Events

On October 1, 1998, the State of Montana issued \$3,065,000 of General Obligation Bonds(Drinking Water State Revolving Fund Program), Series 1998F, to finance and refinance drinking water facilities or improvements.

The Interentity loan of \$350,000 for the DWSRF program was repaid in August 1998.

DWSRF loan disbursements through February 1999 totalled \$4,950,814.

17. Year 2000 Issue

The Year 2000(Y2K) issue is the result of shortcomings in many electronic data processing systems and other electronic equipment that may adversely affect the operations of the program beginning January 2000. Many computer programs use only the last two digits when referring to a year. As a result, some computer programs will not be able to distinguish between the year 2000 and the year 1900. This may cause inaccurate processing of information or a complete halt to processing.

The trustee bank, US Bank, has assured us and provided written documentation stating that their computer systems that support the SRF program will be Y2K compliant by January of 2000.

The SRF program does not anticipate any disruption of services as a result of non-compliant internal systems. However, because of the unprecedented nature of the Y2K Issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that Montana is or will be Y2K ready, that the remediation efforts will be successful in whole or in part, or that parties with whom Montana does business will be Y2K ready.

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel
Tori Hunthausen, IT & Operations Manager



Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

To the Legislative Audit Committee
of the Montana State Legislature:

Our audit was made for the purpose of forming an opinion on the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs' financial statements taken as a whole. The Schedule of Revolving and Non-Revolving SRF Program Assets for the Montana Water Pollution Control Program and the related Schedule of Revolving and Non-Revolving SRF Program Revenues, Expenditures, and Changes in Fund Balance are presented for purposes of additional analysis and are not a required part of the financial statements of this program. Such information has been subjected to the auditing procedures applied in the audit of the programs' financial statements and, in our opinion, based upon our audit, is fairly presented in all material respects in relation to the programs' financial statements taken as a whole.

Respectfully submitted,

(Signature on file)

James H. Gillett, CPA
Deputy Legislative Auditor

March 12, 1999

MONTANA WATER POLLUTION CONTROL PROGRAM
 SCHEDULE OF REVOLVING AND NON-REVOLVING SRF PROGRAM ASSETS
 STATE SPECIAL REVENUE AND DEBT SERVICE FUNDS
 REGULATORY BASIS
 JUNE 30, 1998

	WATER POLLUTION CONTROL SPECIAL REVENUE		WATER POLLUTION CONTROL DEBT SERVICE		(FOR MEMORANDUM ONLY) TOTAL
	SRF REVOLVING	SRF NON-REVOLVING	SRF REVOLVING	SRF NON-REVOLVING	
Cash/Cash Equivalents	\$1,537,812	\$140,472	\$361,321	\$104,310	\$2,143,915
Due From Other Accounting Entities	10,618				10,618
Interest Receivable		81,491	337,859		419,350
Investments	10,471,591	1,429,775		1,069,692	12,971,058
Loans Receivable	35,510,667				35,510,667
Total Assets	<u>\$47,530,688</u>	<u>\$1,651,738</u>	<u>\$699,180</u>	<u>\$1,174,002</u>	<u>\$51,055,608</u>

LIABILITIES AND FUND BALANCES

Liabilities:

Deferred Revenue	\$233,463	\$233,463
Accounts Payable	373	373
Due to Other Accounting Entities	17,818	17,818
Total Liabilities	<u>251,654</u>	<u>251,654</u>

Fund Balances

Reserved for Loans Receivable	35,510,667	35,510,667
Unreserved, Undesignated	11,768,367	15,293,287
Total Fund Balances	<u>47,279,034</u>	<u>50,803,954</u>
Total Liabilities and Fund Balances	<u>\$47,530,688</u>	<u>\$51,055,608</u>

1

This schedule is prepared on a regulatory basis of presentation instead of a GAAP basis as requested by the Environmental Protection Agency for the Water Pollution Control Program. The regulatory basis of presentation separates certain regulated SRF revolving financial activity from SRF non-revolving activity by fund type. All proceeds from the EPA Capitalization Grant and corresponding state match monies, and all loan principal and interest repayments must be deposited into the Revolving Fund under Title VI of the Clean Water Act. Other proceeds, including Administration and Origination Fees and the Loan Loss Reserve Account, are deposited into the Non-Revolving fund and may be used for other water quality purposes under the Clean Water Act.

¹ Generally Accepted Accounting Principles (GAAP).

MONTANA WATER POLLUTION CONTROL PROGRAM
 SCHEDULE OF REVOLVING AND NON-REVOLVING SRF PROGRAM REVENUES, EXPENDITURES,
 AND CHANGES IN FUND BALANCE
 STATE SPECIAL REVENUE AND DEBT SERVICE FUNDS
 REGULATORY BASIS
 FOR THE YEAR ENDING JUNE 30, 1998

	WATER POLLUTION CONTROL STATE SPECIAL REVENUE		WATER POLLUTION CONTROL DEBT SERVICE FUND		(FOR MEMORANDUM ONLY) TOTAL
	SRF REVOLVING FUND	SRF NON-REVOLVING FUND	SRF REVOLVING FUND	SRF NON-REVOLVING FUND	
REVENUES:					
Federal Capitalization Grant Revenue	\$5,864,005				\$5,864,005
Interest Income on Investments	558,691	\$84,741	\$55,640	\$17,260	716,332
Interest Earnings		246,757	845,862	199,697	1,292,316
Administration and Origination Fees	126,456				126,456
TOTAL REVENUES	6,549,152	331,498	901,502	216,957	7,999,109
EXPENDITURES:					
Program Administration	261,691				261,691
State In-Kind Services-RIT	10,853				10,853
TOTAL EXPENDITURES	272,544	0	0	0	272,544
Excess Revenues Over/(Under) Expenditures	6,276,608	331,498	901,502	216,957	7,726,565
OTHER FINANCING SOURCES:					
GO 98A Bond Proceeds	3,510,000				3,510,000
<i>Operating Transfers In:</i>					
RIT Transfers In	10,853				10,853
Administration and Origination Fees		46,166		80,290	126,456
GO Bond Cost of Issuance		105,431			105,431
Arbitrage Rebate Transfers				31,575	31,575
Debt Service Sweep	109,889				109,889
Total Other Financing Sources	3,630,742	151,597	0	111,865	3,894,204
OTHER FINANCING USES:					
Bond Principal			200,000		200,000
Bond Interest			409,429		409,429
Bond Cost of Issuance		96,773			96,773
<i>Operating Transfers Out:</i>					
Debt Service Sweep			109,889		109,889
Administration and Origination Fees	126,456				126,456
GO Bond Cost of Issuance	105,431				105,431
Arbitrage Rebate Transfers	26,055	5,520			31,575
Total Other Financing Uses	257,942	102,293	719,318	0	1,079,553
Excess(deficiency) of revenues and other financing sources over(under) expenditures and other financing uses	9,649,408	380,802	182,184	328,822	10,541,216
Fund Balance - July 1, 1997	37,608,687	1,270,936	516,996	845,180	40,241,799
Prior Period Adjustments	20,939				20,939
Fund Balance - July 1, 1997--As Restated	37,629,626	1,270,936	516,996	845,180	40,262,738
Fund Balance - June 30, 1998	\$47,279,034	\$1,651,738	\$699,180	\$1,174,002	\$50,803,954

¹ This schedule is prepared on a regulatory basis of presentation instead of a GAAF basis as requested by the Environmental Protection Agency for the Water Pollution Control Program. The regulatory basis of presentation separates certain regulated SRF revolving financial activity from SRF non-revolving activity by fund type. All proceeds from the EPA Capitalization Grant and corresponding state match monies, and all loan principal and interest repayments must be deposited into the Revolving Fund under Title VI of the Clean Water Act. Other proceeds, including Administration and Origination Fees and the Loan Loss Reserve Account, are deposited into the Non-Revolving fund and may be used for other water quality purposes under the Clean Water Act.

¹ Generally Accepted Accounting Principles (GAAP).

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel
Tori Hunthausen, IT & Operations Manager

Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
James Gillett, Financial-Compliance Audit



INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Legislative Audit Committee
of the Montana State Legislature:

We have audited the financial statements of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs as of and for the fiscal year ended June 30, 1998, and have issued our report thereon dated March 12, 1999. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. However, we noted certain immaterial instances of noncompliance, which we have discussed with management.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Departments' (Department of Environmental Quality and Department of Natural Resources and Conservation) internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be a material weakness. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that a misstatement in amounts that would be material in relation to the financial statements being audited may occur and not be detected in a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its

operation that we consider to be a material weakness. However, we noted other matters involving the internal control over financial reporting, which we have discussed with management.

This report is intended for the information of the Legislative Audit Committee, department management, the Montana State Legislature, and the U.S. Environmental Protection Agency. This report is a matter of public record and its distribution is not limited.

Respectfully submitted,

(Signature on file)

James H. Gillett, CPA
Deputy Legislative Auditor

March 12, 1999